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THE MAIN EFFECTS OF THE MIDDLE EAST WAR

REPORT BY JOINT INTELLIGENCE COMMITTEE (A)

*Cabinet Office,
London*

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JOINT INTELLIGENCE COMMITTEE (A)

THE MAIN EFFECTS OF THE MIDDLE EAST WAR

Report by the Joint Intelligence Committee (A)

The attached report was approved by the Joint Intelligence Committee (A) at its meeting on THURSDAY 5 DECEMBER 1973. In view of the complex and fluid nature of the new situation created by the Middle East war and the intrinsic importance of the subject the report is issued without a summary.

Signed LOUIS W. BAKER
Acting Chairman on behalf of the
Joint Intelligence Committee (A)

Coldest Office

3 December 1973

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THE MAIN EFFECTS OF THE MIDDLE EAST WAR

Introduction

This paper seeks to assess the changed situation and the outlook in the Middle East in the light of the recent war and to consider some of the principal implications, in particular those relating to oil supplies. Although concentrating on the Middle East, it takes account of a number of wider factors operating in the new environment, including US and Soviet policy in the Middle East, the US/Soviet relationship, and the effect of the war and the oil crisis on relations between the US and Europe.

2. The paper is concerned mainly with the next 2 or 3 years but it looks further ahead on certain aspects, in particular the question of future oil supplies.

3. A paper of this scope is inevitably in very generalized terms: specific aspects may well require more detailed separate study. It is also inevitably tentative in its conclusions: the situation is complex, fluid and subject to sudden change.

PART 1: THE MIDDLE EAST. TWO SCENARIOS

The Current Situation

4. Very briefly the following are the salient features of the current situation -

- a. The war ended with Israel, having recovered from the initial surprise Arab attack, on the verge of a considerable military victory. She had established control of a large area of Egyptian territory on the west bank of the Suez Canal. Many of Egypt's air defence sites had been destroyed and in the closing stages of the war Israel enjoyed almost complete air superiority over the Canal front. The prospect was of the progressive isolation and destruction of Egyptian forces on the east bank. On the Syrian front the Israelis reconquered the territory gained in 1967 and also a large area south west of Damascus

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and north east of Damascus. The Syrian forces, supplemented by Iraqi, Jordanian and Saudi Arabian elements, were not destroyed but suffered heavy losses in manpower, aircraft and armour. Moreover Syria's infrastructure had been severely damaged as a result of Israeli air attacks on ports, power stations and refineries. On the other hand Israel's losses were severe, particularly in manpower, and her high level of mobilization was such that it could even imperil her economy in any protracted war. In brief, Israel was on the road to victory but had paid dearly. Egypt, though facing defeat, was still able to claim a measure of success in having repulsed some of Israel and had at least delayed the myth of Israeli invincibility. The Syrians had suffered heavy losses but could still deny that they had been defeated.

b. The war was brought to an end principally as a result of superpower intervention. The Americans and Russians supported their clients during the war with large quantities of military equipment; but throughout they maintained their communications with each other and attached particular importance to the US/Soviet relationship, although this inevitably came under strain. When each side for its own reasons judged the time ripe, they were able to reach agreement on a ceasefire with considerable speed. The relationship later suffered particular strain as a result of Israeli military activity following the first ceasefire and Soviet unwillingness to see the Egyptians humiliated; nevertheless, despite Soviet pressure for joint US/Soviet intervention and the US alert on 25 October to meet what the Americans saw as the threat of unilateral Soviet intervention, the relationship holds and both parties are anxious to preserve it. Mr Brezhnev in his speech on 25 October continued to lay stress upon detente and on the US/Soviet relationship elaborated over the previous 2 years and both Americans and Russians have recognized the need for progress towards Arab/Israeli negotiations and eventually a settlement.

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3. Security Council Resolution No 136, which brought about the initial ceasefire, provides for the implementation of Security Council Resolution 242 of 1967 and negotiations "under appropriate auspices" aimed at a just and durable peace. Ideally, therefore, there should soon be Israeli/Arab negotiations and there is now some prospect of these beginning in December. However, despite the truce signed by Egypt and Israel on 11 November, there are clearly a number of points (notably a prolonged suspension of the Km 101 talks) which could cause the truce to break down. Furthermore, such contacts as there have been between Israel and Syria have not been encouraging.

4. The war provided the Arabs with the oil weapon. There were already economic arguments inducing them to restrict output and certain States were already doing so, but it was the war which brought collective action in support of political and military objectives. The Arab oil producers announced on 17 October their decision to cut their oil production by a monthly minimum of 5 per cent of September levels. Subsequently most producers announced a 10 per cent cut and later decided that they would also embargo exports to selected countries, notably the US and the Netherlands. At their meeting in Kuwait on 4 and 5 November the Arabs decided that the total embargo should be 25 per cent, inclusive of quantities involved in the US and Dutch embargoes, "provided that no reduction shall affect the share which any friendly State imported from any Arab oil-exporting State during the first 9 months of 1973". These restrictions were to apply until the end of November. At a meeting in Vienna on 10 November, the Arabs seemed to agree that "in appreciation of the political stand taken by the Common Market countries" they would not further penalize those countries, except for the Netherlands, in December, but that they would not supply elsewhere in that month and continue to apply the embargoes on the Netherlands and the US. The 10 November announcement also envisaged a further 5 per cent cut in production in January, possibly with certain unspecified exceptions. This general policy was endorsed by the Arab Summit conference at Algiers on 26-28 November; but its probable effects are still uncertain.

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e. Some of the Arab producers have stated that they will maintain restrictions until a satisfactory Arab/Israeli settlement, including recognition of the claims of the Palestinians and, in the case of Saudi Arabia, satisfaction over the status of Jerusalem, is achieved; in any event it seems likely that restrictions in some form will be maintained, or periodically reimposed, until there is a settlement. It is, however, difficult to assess the practical effect of the various Arab oil measures, and of the measures of preferential treatment for "friendly countries", given the complexity of the distribution system of the international oil industry.

f. The war has damaged relations between the US and its European allies and highlighted longstanding differences in their Middle East policies. The principal irritants have been US annoyance at European failure to give greater assistance to the US in resupply of military equipment to Israel; European complaints over lack of consultation throughout the crisis and especially before the US alert of 25 October; and European failure publicly to endorse US action in declaring that alert. The oil shortage and US/European/Japanese competition for oil in a tight market could produce further difficulties, as could European resentment that although not the principal target they are likely to be (with Japan) the principal victims of the Arab oil restrictions. These factors, added to existing frictions over trade relations between the US and the Community, European defence questions (including burden-sharing), and Dr Kissinger's proposal for a new declaration of Atlantic principles, have threatened a general deterioration in transatlantic relations. US spokesmen have openly criticized NATO and suggested that the current climate over the Middle East could adversely affect the US attitude to the maintenance of US troops in Europe.

g. The war and the resulting oil restrictions have strained Community solidarity. Although the Europeans, in company with the Japanese, have had to look for any interference with Middle East oil supplies, they were unable to agree among themselves about their Middle East policies and in any case were not in a position to intervene effectively in the earlier stages of the crisis. The two superpowers held, and

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still hold, both the stage and the key. In their declaration of 4 November the Nine were able to adopt a common position on the Middle East, but the Arab embargo on oil supplies to the Netherlands, the related possibility of Dutch restrictions on gas exports to their European partners, and the prospect of increasing competition among Europeans for scarce oil resources raise serious questions as to the future of European unity.

The Outlook in the Middle East

5. The principal determinant of the Middle East and hence the wider world will be the pace and extent of movement towards an Arab-Israeli settlement which most Arab States are prepared to accept. Put in very broad terms, if there is some early movement in this direction from the ceasefire, the Middle East situation will improve though it is too much to hope that all restrictions will be abandoned. If, however, there is no such movement, with the result that the ceasefire is seen as simply formalising Israeli military gains in a highly unstable situation, then we must expect an early deterioration. We are therefore concerned in the following section with two broad scenarios, which we shall call the bright and the dark. It should be borne in mind that these two scenarios simplify for purposes of analysis a situation in which there is, strictly speaking, a whole spectrum of possibilities, ranging from the uncomfortable to the very serious. The terms used are relative in this context "bright" is a case for "grey". Moreover, as noted in paragraph 26, the two scenarios could merge.

The Bright Scenario

6. The essentials of this are that under superpower persuasions, there would be early negotiations between the Arabs and Israelis accompanied by phased Israeli withdrawals. These withdrawals would be in the first instance back to the neighbourhood of the first ceasefire line in accordance with the terms agreed on 11 November. There would later have to be withdrawals by the Israelis from the west bank of the Canal and eventually from a large part of Sinai in return for guarantees of secure frontiers. Similar arrangements, involving Israeli withdrawals and guaranteed frontiers might be possible in the north in the Golan Heights; agreement would be necessary on the competing claims of Jordan and the Palestinians, and Israeli Arabs would have to be satisfied over the status of Jerusalem.

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The ultimate conclusion might be a settlement acceptable to Egypt, and Syria, and in which Jordan might have to acquiesce, although it might not be acceptable to the Palestinians, or perhaps to Libya and Iraq.

7. If there were such progress towards a settlement we might expect an intensification of the Arab oil restrictions. We cannot be sure of this: there might for example be some tightening at difficult sticking points, eg the Israeli withdrawal from the west bank of the Canal without Egyptian withdrawal from the east bank, or at some later stage over such issues as the Golan Heights and Jerusalem. Some Arab States may envisage further 5 per cent cuts until Israel withdraws to the 1967 frontiers. Nevertheless there would be a good chance of no worsening in the oil situation; continued concessions for Europe might be possible. There could even be some slackening of oil restrictions and some Arab States may practice less than they preach. But on present evidence the most realistic prediction is that in a state of deadlock towards a settlement the Arab oil restrictions would be maintained though not intensified. This could mean a long period of difficulties over oil; under the most hopeful supposes a settlement will not be rapidly achieved. Kissinger is reported as saying he will need 6 months or a year to arrive at the beginnings of a reasonable solution.

8. In such a situation of progress we might also expect too if any internal changes in Arab regimes. Hussein would be under no new threat. Faisal would be able to retain his Western links and avoid getting too deeply involved with the Baathists. Faisal and Assad would be able to refer any domestic crises to fruitful negotiations (though such references would be unlikely to satisfy the more militant Palestinians). The extremists, such as Qaddafi, would probably remain isolated.

9. The influence of the US and the Soviet Union with the Arabs would be high under such conditions since they would be seen as the principal sources of negotiating benefits. An actual settlement would greatly increase US influence with the Arabs. Both the Baathists and the Americans, if they

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as claimed, could claim that their bilateral co-operation had produced results in a crisis, and there would be a widespread tendency to see this co-operation as providing the answer to other world problems. The Russians would retain certain assets - their record of help to the Arabs, an enhanced degree of respectability (as with Poland) and the continuing needs of military and economic aid. But these assets would be less valuable in a more unified Arab world. Arab nationalism and general dislike of the Russians would weaken Soviet influence. The US and Europe would be seen as more attractive sources of assistance. European trading links with the Middle East could rapidly develop, and host of the Arabs would become more responsive to the West.

18. But there will have been a fundamental change in the Middle East oil scene. The Arabs will not have forgotten the power brought them by oil and would be tempted to use the oil weapon again either in support of further demands against Israel or in some third world cause. Even after a settlement some of them will have good conservationist and financial arguments for maintaining some restrictions on oil output. The influence of the international oil companies will be significantly weakened. To foresee that in the next few years Arab oil supplies will not only be subject to restriction, but very much harder than in the past. The consequential balance of payments implications will mean that consumer countries will have to revise all their economic objectives and capabilities, both internal and external. In particular, they will have to find ways of adjusting themselves to the new situation while avoiding measures likely to make a potentially inflationary situation worse. Furthermore, a continued increase in the great financial power of the Arab oil producers will in itself affect the attitudes to Arab interests of the industrial West.

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The Dark Scenario

11. Under this scenario we assume that movement from ceasefire to settlement fails, almost certainly because Israeli withdrawal cannot be achieved or maintained.

12. In this event we must expect a marked and rapid deterioration in the Middle East situation, with a risk of renewed fighting. If the breakdown occurred in the near future new large-scale fighting on the Golan front would be likely. The Egyptians and the Syrians have probably received by now sufficient supplies of equipment from the Soviet Union to repair losses during the war, although they may need time to train back and fill out replacements. For their part, the Israelis may be inhibited by the risk of further heavy equipment losses. Nevertheless, if fighting were resumed, the most likely outcome would be for the Israelis to inflict heavy damage on the Egyptians before the superpowers could again impose a ceasefire. The Syrians might also resume fighting; again we would expect Israeli success, though perhaps not a decisive victory.

13. A new outbreak of fighting would impose further strains on the US/Soviet relationship. If, as is likely, the Egyptians suffered further heavy losses, and, a fortiori, if the Egyptian armed forces were threatened with destruction, the Russians could once again face heavy Arab pressure to intervene. We would expect in the first instance renewed Soviet pressure on the US to force the Israelis to halt: we would also expect the Russians to propose once again a joint US/Soviet force, and we cannot rule out the possibility that in these circumstances the US might agree. If the US failed to stop the Israelis and refused to participate in a joint force, there would be a possibility of the unilateral dispatch of Soviet troops to Egypt despite the notice served by the US in October that they would not tolerate this. We recognise that this would be the worst case, and would probably lead to a breakdown of the US/Soviet relationship, and consequential movement of US troops to Israel. On balance, we do not believe that the situation could deteriorate to this extent. We believe that even in this extreme situation the Russians would continue to give greater importance to

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permitting a direct confrontation with the US and to their Westpolitik then to recruiting their clients in the Middle East, and that the superpowers would succeed after some time in reimposing a ceasefire. But the choice for the Russians would be harder on this occasion; and the chances of a joint US/Soviet intervention would be greater.

14. A breakdown at a later stage in the process from ceasefire to settlement, or after Israeli withdrawal from the west bank of the Canal, would carry less risk of an immediate resumption of hostilities. But a prolonged stalemate, amounting in effect to a return to the post-1967 "no peace, no war" situation, would produce a dangerous inflation of Arab frustrations and a corresponding risk of regional renewed hostilities. To consider this perhaps the most likely variant of the Arab scenario. Rather than war now fighting or not we must expect in this situation greatly intensified all restrictions and possibly accelerated price increases, and we must expect a high degree of Arab unity in opposing these conditions. The Arab world would become generally more extreme and its mood would be violently anti-US and by extension anti-East. Any regime which tried to win against the tide of anti-American feeling might well be overthrown. In such a situation it is questionable whether the Arabs could continue to discriminate in favour of friendly European countries.

15. In a situation of this kind US influence in the Arab world would greatly diminish since the failure of negotiations would be attributed by the Arabs to US inactivity or unwillingness to bring the necessary pressure on Israel. The effect on Soviet influence could depend largely on the course of any new outbreak of fighting and the timing of any further superpower intervention. If, as is more likely, the Arabs were the main sufferers, the Russians would benefit by securing intervention to halt the Israeli advance. If, on the other hand, the Arabs were pursuing a successful war of attrition, Soviet involvement in another imposed ceasefire would be to the detriment of Soviet influence since it would be clear that the Russians were getting their relationship with Washington above that with the Arabs. In a situation in which negotiations break down, but without involving new fighting - a new stalemate - the Russians should be able to maintain their relationship with Washington at the same time as making considerable gains in influence in a very dissatisfied and anti-Western Middle East.

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Which scenario?

16. There are some grounds for optimism. Both the US and the Soviet Union have a great interest in a more stable Middle Eastern and international situation and are seriously engaged in the pursuit of negotiations and an acceptable settlement. Each is in a position to bring pressure on its client, particularly given the need for diplomatic support and for new supplies of military equipment on each side. Dr Kissinger has said he is ready to apply major pressure on Israel and there is evidence that some pressure has already been successfully applied to bring about the cease agreement of 11 November. The US is also able to bring influence on side of the Arabs. A new US/Egyptian relationship has been created by the war; the Egyptians will be anxious to preserve this and, like many other Arabs, would prefer to deal with the US, rather than rely too heavily on the Soviet Union. Throughout the crisis Israel has proclaimed only limited objectives and it is likely that if Israel could be persuaded to return to something like 1947 frontiers, the main Arab parties would be content.

17. Unfortunately there are also strong grounds for gloom. The movement from ceasefire to settlement ran at once into a major snag - the problem of the Israeli PFFs and the Egyptian 3rd Army - and although these difficulties have largely been resolved they are illustrative of a problem which will recur again and again on the road to a settlement. Even if Israeli/Egyptian matters are settled there remain intractable issues involving Syria, Jordan and the Palestinians. The Israeli Government are under right wing criticism and are already planning the inhibiting effects on their negotiating position of their imminent general election. It is at best questionable how far any likely future Israeli government would be prepared to make the further concessions needed to permit a settlement within the terms of Security Council Resolution 242. But Israeli concessions will be needed all along the line. It is even then and the Americans that the major snag must arise: the principal Arab states concerned have already expressed or implied their unwillingness to make most of the concessions required of them under Resolution 242. Again it is uncertain whether the US Government will be able to apply the continuous backbiting pressure that will be needed to overcome Israeli intransigence, given the strength of the Zionist lobby inside the US and the precarious domestic position of the President. Although we all agree that the chances of a settlement are better now than at any time in the past, we cannot give the bright scenario more than an even chance - and even of us give it considerably less than this.

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POINT 2: THE LONG-TERM FUTURE FOR OIL SUPPLIES AND ITS IMPLICATIONS

10. The foregoing analysis suggests that we are likely to be faced with reductions in Arab oil production continuing over a long period. In the more hopeful situation the Arabs might maintain production at the present level while continuing preferential treatment and OEC exemptions as far as possible (there is, however, some uncertainty about the latest Arab moves - see Paragraph 4(d) above). This would nevertheless bring production more than 25 per cent below the pre-war level. Restrictions are likely to be maintained until a settlement is achieved, though there could be variations in the level depending on progress in the negotiations. We cannot be sure when a settlement might be reached but a year would seem the minimum period required. In the darker scenario we would expect at least a continuation of roughly 5 per cent cuts, with perhaps some withdrawal of exemptions and probably more intense and protracted restrictions on production.

11. Will the Arabs be able to maintain prolonged restrictions of this kind? There are arguments that they will not. Traditionally they have lacked the capacity to hold together for long periods or to concentrate on a single objective. Some Arab Governments need the revenue; others, such as Abu Dhabi, are inherently inclined. There may be points on the road to a settlement when in view of progress made some Arab leaders will wish to relax pressure and shed the heat some of the current heat of the stick. Indeed, for example, my feel inclined to wait as his leave if he can secure Israeli withdrawal from the west bank of the Canal while retaining an Egyptian presence in Sinai. In any event the Arabs must realize that they are hurting Europe more than the US. The latest Arab statements on oil show a willingness to target the restrictions in the case of most OEC countries. It is not in Arab interests to have a weakened Western Europe or, for that matter, a generally more unstable world. Despite their higher revenues from increased prices, the demand economic spiral their restrictions are setting in motion will before their present wealth and their long-term prospects. They do not wish to be over-dependent on the Soviet Union. They are aware of the fundamental importance of their ties to the Americans if a negotiated settlement is ever to be achieved and will realize that this could be threatened by protracted oil restrictions.

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20. As against this the Arabs have spent all predictions by their solidarity and determination since the outbreak of the war. They have taken the plunge in using the oil weapon and are satisfied to see in Europe, Japan and perhaps also in US behaviour evidence that it works. Eisenhower has said he will not assist negotiations when under pressure over oil but this is just what he is doing. Progress towards a settlement may be seen by some Arabs as ground for relaxing restrictions; but others may see it as a reason for maintaining pressure. Israel is probably a motorist in this context, but he does not control the oil. The paradox of the present situation is that traditionalist regimes such as Saudi Arabia and Kuwait could become the extremists over oil (while Iraq, a political extremist, is the only Arab oil producer not to apply restrictions). Israel is currently showing great rigidity and he and the Saudis have good economic grounds for restricting production in any event. Increases in price, in particular the unilateral increases imposed at the beginning of the war, put the Arabs in the happy position of receiving increased revenues from a smaller quantity of oil. On the wider question of damage to the world economy, the Arabs no doubt realize that in an interdependent world there is a limit to the pressure they can exercise without hurting themselves, but on the subject of Israel they are not very rational; and in any case they are likely to over-estimate the capacity of Europe to influence the US or to take the squeeze. They may also fail to realize until too late the seriousness of the forces their action could set in motion. However, in the dark scenario, to which we give at least as even chance, they are likely to feel particularly resentful and desperate and could become so committed to the use of oil as a weapon that they could not retreat and would apply it in a spirit of emotion and revenge.

21. On balance, therefore, we consider that the Arabs are likely to maintain their restrictions until they achieve a settlement they consider satisfactory and that it is reasonable to pursue the enquiry on the assumption of such continuing restrictions.

22. In the following section we examine further some of the implications of the bright and the dark scenarios for Western Europe, the US, Japan and the Soviet Union.

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Implications of the Bright Scenario

23. About 60 per cent of Western Europe's energy requirements are met from oil imports, of which about two-thirds have hitherto come from the Arab countries. The Arab oil producers have thus been meeting about 40 per cent of Western Europe's energy needs. On the basis of the cuts in production announced so far, Western Europe as a whole (excluding the Netherlands) could be suffering oil supply shortfalls of up to 20 per cent. But, despite the measures taken by the international oil companies to equalize distribution, the ban on shipments to the Netherlands means that those countries (notably Germany and Belgium) which depend to a significant extent on the supply of crude and refined products through Rotterdam may be facing larger shortages. The measures taken so far by governments to meet the shortfalls mainly affect domestic and commercial users, who depend on oil for about half their needs and normally take roughly one quarter of supplies. Other measures to conserve stocks could soon be necessary if serious economic dislocation is to be avoided. These would be bound to involve cuts in supplies to other sectors, including transport, which is nearly 100 per cent dependent on oil.

24. The United Kingdom should be rather better placed than most West European countries both because of our developed coal industry and possibly also because of the assurances of preferential treatment which we have received from certain Arab Governments. It is still not clear, however, to what extent these assurances can be given practical effect in view of the complexity of the world oil distribution system. It is possible that the effects of oil restrictions on the United Kingdom could be further mitigated if we were successful in our present endeavour to persuade the Arabs to allocate more oil to the United Kingdom at times of seasonal need than they had originally intended. As against this, we cannot be confident that we will continue to be regarded as worthy of any favored treatment. The Arabs may decide to work out a system like in which the majority might wish to apply greater pressure on Europe and Japan. There could be criticism of the United Kingdom by individual Arab countries, for example on the United Kingdom record over the Palestinian issue or on other real or imagined grievances. There might also come a point where we could not entirely neglect claims for assistance from our European partners.

25. A situation of this kind is likely to involve continued strains between the United States and Europe. The Europeans are likely to wish to maintain the marginally pro-Arab policy typified by the 4 November declaration and will hope that this, coupled with statements in support of a settlement which the Arabs could accept, will be sufficient to convince

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the Arabs that preferential treatment should not only continue but should be extended to other Europeans, including the Dutch. If this policy failed the Europeans could come under pressure to adopt more openly pro-Arab policies. The Americans for their part are so far relatively unaffected by the Arab embargo on oil exports to them, since this involves a shortfall of only some 17 per cent in US supplies, or about 6 per cent of their overall energy supplies. They will proceed with their efforts to bring about a settlement, and will no doubt claim that they are working in the common Western interest and therefore deserve greater European backing. These US/European strains should however be manageable in the circumstances envisaged.

26. Equally this is likely to be a situation of continuing strains on European solidarity as countries seek to protect their own interests. Both the United Kingdom and France will have reasons for seeking to maintain their preferential arrangements and to avoid too obvious efforts to mitigate the loss of their European partners. If, however, for one reason or another preferential treatment proves impracticable or is abandoned, this would permit more practical demonstrations of European solidarity.

27. Japan is likely to be hard hit even in this best of cases. Japan imports 35 per cent of her rapidly-growing oil needs and in 1972 43 per cent of these imports came from Arab countries, representing about 32 per cent of her energy requirements. The Japanese Minister for Industry forecasts a zero or even negative rate of growth for the Japanese economy from the end of this year if Arab measures remain in force: since the economy has been geared to about 10 per cent annual growth, such a change would cause particularly serious problems. On 22 November the Japanese Government issued a policy statement favourable to the Arabs; the latter have since said that they will exempt Japan from the 5 per cent cut in December oil shipments. Yet further pressures may be applied to induce Japan to adopt more strictly anti-Israeli policies. Since a major move in this direction could create problems for Japanese/US relations, Japan may be reluctant to go further in public than statements on UN lines, while seeking to convey greater support privately to particular Arab Governments. The Japanese will also seek direct deals with oil-exporting countries and will intensify their efforts to diversify sources, by seeking oil guaranteed supplies from Indonesia and Nigeria. These moves could result in a deterioration in Japan's relations with Europe as well as the United States.

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28. Oil restrictions of the kind envisaged under this scenario, together with price increases, would be likely to mean a loss of growth and marked reductions in economic prospects for Western Europe and Japan as well as adding to inflationary pressures. They would also be likely to involve major inconveniences but would not necessarily mean more fundamental change or instability. It should be emphasized however that we are here assuming that restrictions do not become more severe after December. If the Arabs were to continue to reduce production by a further 5 per cent a month after December (although this is unlikely under the bright scenario), this would mean an overall loss in Arab oil production reaching at least 10 million barrels a day next May. Since Arab production was previously expected to rise to an average of about 26 million barrels a day in 1974, the loss would in practice be even greater, perhaps getting on for 13 million barrels a day or nearly 60 per cent of production. Given Europe's dependence on Arab oil supplies, it is likely that after 4 months of progressive cuts of this kind there would be a situation of major economic crisis and probably mass unemployment. Japan would also of course be severely affected. In other words, given progressive cuts after December we should even under the bright scenario be moving toward a situation of major crisis and the two scenarios would at this point begin to merge.

Implications of the Dark Scenario:

29. We are here envisaging intensified and protracted oil restrictions. We should emphasize that here we are moving into a situation in which many familiar aspects of the international situation would be likely to change. The crisis has already threatened United States/European relations and solidarity within the Community. But protracted restrictions under the dark scenario could provoke more profound and even violent change, including a rupture of Western European and Japanese economies and instability within Western and Third World societies.

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UN Attitudes

10. A factor of crucial importance would be the US attitude. The total Arab embargo on oil deliveries to the United States has so far meant a shortfall of 17 per cent in US supplies; this should be manageable for the Americans. But they had planned to increase imports from Arab sources to meet the needs of economic growth; and if it became clear that the embargo was likely to continue long enough seriously to affect the prospects of growth, the US Government would come under increasing pressure to secure its removal. Moreover they would be deeply concerned over the threat posed by prolonged oil restrictions to the economic and political stability of Western Europe, Japan and other friendly countries, and the US economy would suffer from the recession elsewhere in the industrial world. The US Government would see a threat to US interests generally. The Americans would be likely to bring greater pressure to bear on any weaker brethren among the Arab oil producers. But effective counter-measures against Arab balances or exports to Arab countries (already being talked about in the US) would present many practical problems; they would require agreement among and simultaneous action by all major Western governments; and the Arabs would still retain the sanction of yet more stringent cuts in oil supplies to the West.

11. The breakdown of movement towards a settlement would almost certainly arise from Israeli intransigence and US inability or unwillingness to apply the necessary pressure upon Israel. The Americans would probably seek in the first instance to attach some blame for the failure on the Arabs or the Russians. They might also seek European assistance in bringing pressure on the Arabs for concessions to satisfy the Israelis; and although the Europeans might be prepared to urge greater flexibility on the Arabs, they would want this to be coupled with further pressure on Israel. There could be severe European/US strains in consequence. The Americans might in the end be faced with a choice between forcing the Israelis to make the necessary concessions or attempting to seize and operate selected Arab oilfields. Despite Zionist influence in the US, extreme pressure on Israel - in effect imposing a settlement - would be likely to appear less despicable to the US Government in the circumstances envisaged than it does now. It could

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to come by than as preferable to seizure of Arab oilfields, a course involving major military action, total alienation of the Arabs and the risks of a third world war. Nevertheless there are reasons for fearing that this latter course (ie attempted seizure of Arab oilfields) might be chosen. In the first place, in a developing and complex situation the choice between coercion of Israel and a seizure of Arab oilfields could present itself less starkly to the US Government than as suggested in the passage above. In the face of Israeli intransigence the US Government might lack the political will to apply the ultimate pressure necessary to secure Israeli compliance. The US Government might also feel it necessary to show that the United States and its allies could not tolerate a situation where they were at the mercy of a small group of Arab States. In a situation where, as they would assume, no more concessions from Israel were attainable or reasonable, and where all other steps to have the oil embargo removed had failed, the threat to their other interests and ultimately to the US itself could in the end cause them to consider seriously using threats of force, or using force itself to seize oilfields in Saudi Arabia and the Gulf, despite their reluctance after Vietnam to engage in such operations. They would claim, not unreasonably, that such action was to protect European and Japanese interests and ought therefore to receive full NATO and Japanese support.

32. Either threats of force or, a fortiori, the actual use of force would, of course, be a highly dangerous policy with incalculable consequences. And although the US are likely to have made contingency plans for such an operation, it is most unlikely that these could be put into effect without the Russians receiving some advance warning. Arab sabotage of the oil installations in question would be almost certain, although this might not succeed in preventing the occupying forces from starting production again before long. But if the Americans used force in a single Arab country, a total ban on deliveries of Arab oil to the West would be virtually certain and the Arabs would try to persuade other producers, notably Iran and Nigeria, to follow suit.

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Western Europe

11. The Europeans would be badly torn as this situation developed. Their immediate inclination might be to seek to protect their Middle East interests and oil supplies by adopting more openly pro-Arab attitudes. If, after a breakdown in negotiations, the Arabs sought UN support for sanctions against Israel, it is arguable that the Europeans might eventually vote for such resolutions, even in the face of a US veto. But the Europeans could not be sure that this policy would mollify the Arabs and ensure oil supplies in the eventual circumstances then prevailing. Moreover as the situation worsened there would be strong conflicting pressures in European countries. On the one hand various factors would make for a tendency to move closer to the United States and even, in extreme circumstances, to consider the possibility of force. Such factors could include a wish to support European partners suffering particularly from Arab restrictions, an unwillingness to appear to be appeasing the Arabs, and the likelihood of increasing Arab demands upon Europe, eg to cut off remittances to Israel. Pro-Israeli groups would be extremely active in the West; the Arabs would be popularly presented as in league with the Soviet Union and public opinion would harden against substantial concessions to the Arabs. On the other hand, other factors could encourage support for further pressure on Israel and impatience with American inability to apply it. If it came to be felt that Israeli intransigence was blocking a settlement and hence was ultimately responsible for the ill effects of Arab oil restrictions, European frustration could turn against Israel and by extension the United States, the more so if the United States Administration were further discredited domestically. But even without any serious upsurge of popular anti-Americanism in Europe, the Five would probably be unable to agree on any strong, pro-American line, particularly one that could involve the use of force; the French, in particular, would be unwilling to associate themselves with the Americans. And notwithstanding European resentment at Arab pressures, unilateral American military action would anger and alarm wide sections of popular opinion in Europe, with damaging consequences for NATO and United States/European relations in general on both sides of the Atlantic.

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Japan

14. The Japanese would probably face problems of policy similar to the Europeans but more severe; eventually they might therefore be ready to close ranks with the Americans. The crisis would in any case have profound political consequences in Japan, perhaps causing the Japanese to question the efficacy of their co-operative and non-militarist policy as a means of ensuring essential raw material supplies and the value of Japan's pro-Western alignment.

The Soviet Union

15. In their attitude to the Middle East the Russians have had to balance two considerations: their wish to pursue their Westpolitik and in particular their special relationship with the United States; on the other hand a wish to maintain and if possible extend their influence in the Middle East. So far they have managed to have their cake and eat it; but they have shown that they give greater weight to their Westpolitik than to their wish to make opportunistic gains in the Middle East. On the whole we think that this attitude will be maintained except in the most extreme circumstances. We think they are likely to continue to watch the Americans very closely, and to bring pressure on the Arabs in order to achieve a tolerable settlement (though the efforts required from them will be much less than the efforts required by the Americans dealing with Israel). They will wish to preserve their influence in the Middle East by maintaining their involvement in all the negotiations leading to a settlement, and to preserve their prestige in the world at large by being seen to be involved on a par with the United States. We think that renewed fighting would present more acute problems to the Russians; but again probably on balance they would give priority to the United States relationship and to considerations of detente and the considerable gains they expect to obtain from this at the expense of the East.

16. On oil the Russians have hitherto played a cautious role. They are not exporters and not importers at the moment and cannot provide a substitute for the industrialized West as a market for Arab oil. They have encouraged the Arab countries to take control of their own resources and have provided technical assistance to some of them. For some time Soviet propaganda has emphasized the potential value to the Arabs of oil as a political weapon and during the war they gave some propaganda support for

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Arab use of it. But it is doubtful whether they wish to play a very active part in this aspect of the problem; they do not need to. Moreover, they would almost certainly see risks to their general policies, and particularly their policy towards the West, if they were even so deliberately engineering an oil confrontation between the West and the Arab world. The Soviet position on the oil issue as far as we can judge it at present is one of active waiting. They see advantages in the frictions produced, particularly between the United States, Europe and Japan, but they do not wish to play a dramatic role.

37. The development of the dark scenario, including tougher and protracted oil embargoes, would be seen by them as a situation of opportunity but also of caution. They will be aware of the advantages their outside position gives them in oil matters. They seek the weakening of Western Europe and the disruption of United States/European relations as part of their policy of shifting the balance of power in their favour. But we see Soviet policy as one of seeking a steady and undramatic erosion of Western strength. They will realize the dangerously destabilizing effects of prolonged oil restrictions. A crisis of the kind envisaged here could, in their eyes, contain dangers of either a sudden removal of Western cohesion or of violent Western action. We do not think that in these circumstances they would seize the opportunity of direct military action against the West; their caution and the uncertainty of the United States response would be sufficient to deter them. Nevertheless, the weakening of Western Europe could increase their opportunities for bringing to bear political pressure backed by superior military strength; the internal debate within the Soviet leadership on foreign and defense policy would become sharper and the advocates of a hard line would be provided with ammunition supporting their case.

38. The shortage of oil in the West might in the longer term give the Russians some opportunities of increasing their influence by exporting more of their own oil, although they might prefer to avoid upsetting the Arabs by increasing their exports significantly. But they will want to be sure that they can satisfy their own needs (and if possible those of their allies) before even considering exports elsewhere. In any case the

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amounts involved would be small in relation to the West's needs, unless the Russians were to resort to crash programmes to develop their own resources, which in turn would require massive financial and technological aid from the West on a scale far greater than appears so far to have been envisaged. Even so it would take several years for a significant flow of oil to be obtained. It is conceivable that the Russians might try to acquire a middleman role, importing large quantities of Arab oil for resale in the West. They would however face severe practical difficulties, even assuming that the Arabs were willing to renounce their obvious desire to exercise direct control over their oil.

35. The most dangerous situation would clearly arise if the West, and particularly the United States, were tempted to use force to seize oil supplies in the Middle East. The Russians would seek to deter the Americans by warnings and alerts such as the United States alert of 25 October. If, nevertheless, intervention occurred, the Russians would be under almost insuperable pressure to give further military assistance to the Arabs and would probably provide it. But we think that they would stop short of direct military intervention against United States forces operating in the oil-producing areas. It is also possible that the Russians would foresee the danger of such a situation developing and would seek to pre-empt it by bringing pressure upon the Arab oil producers to mitigate their restrictions (and if so, they would probably seek some paid arm gun from the West). But certainly, the United States/Soviet relationship and stability generally would be under extreme threat; the situation would be highly volatile and it is impossible at this point to predict the outcome.

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ITEM 3 - LONG TERM IMPLICATIONS

40. We have considered some of the longer-term implications of the present crisis on the assumption that a Middle East settlement is eventually achieved and all restrictions are relaxed.

41. For a considerable time to come the United States and the Soviet Union are likely to remain deeply committed in the Middle East as the principal guarantors of a negotiated settlement. The Middle East and the Mediterranean are thus likely to remain an area of superpower management and the habit of United States/Soviet co-operation to deal with major world crises will be confirmed. Nevertheless, the United States and the Soviet Union will remain the principal protectors of their respective clients; latent Arab/Israeli antagonisms and other potential sources of regional instability, together with the competition for power and influence underlying United States/Soviet collaboration, could give rise to renewed United States/Soviet tensions and possibly confrontations. As recent events have shown, this more permanent superpower involvement in the area will require a more precise definition of the respective rights and responsibilities of the United States and the European members of NATO in crisis situations affecting alliance security but falling outside the strict terms of the North Atlantic Treaty and more effective consultative arrangements for dealing with them. On the whole, as indicated earlier, Soviet influence is likely to be weakened in a more stable and satisfied Middle East, though the Russians will probably be prepared to live with this situation in return for the benefits they expect from their Westpolitik. At the same time US/European relations over the Middle East would have been restored to greater harmony and this, together with a general Arab wish to strengthen ties with Europe, would provide opportunities for the Community to enhance its political and economic influence in the area.

42. However the security situation develops, the crisis has sharply re-emphasized the vulnerability of industrialized Western nations to interruptions in their oil supplies. Having once succeeded in applying this weapon, the Arab oil producers will certainly keep it and the threat

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of large unilateral price increases in their capacity, both as a deterrent to Western actions which they consider contrary to their interests and as a means of bringing active pressure to bear to secure Western acquiescence in policies which they support. They will be aware that the period of their dominance is transitory and that eventually alternative energy sources will be developed. We find it hard to judge whether this will have a moderating influence upon them or will make them even more determined to use their power while it lasts.

43. In any event we think the Arab producers will aim to extend their options by strengthening their control over not only the exploitation but also the processing and perhaps marketing of their oil resources and by diminishing the role and influence of the international oil companies. Western governments too may conclude that they need to control the operations of the oil companies more closely. Just as indicated earlier, the industrialized West will have to adjust to the new situation in which it can no longer rely on plentiful supplies of cheap oil to meet the increased energy demands of economic growth and in which the Arab oil producers are able to wield greatly enhanced financial power.

44. What the Arabs have done may encourage the threatened or even the actual use of the oil weapon by other oil producing states and also for other reasons than the Arab/Israeli dispute. The remarkable degree of anti-Israel solidarity which the Arabs have been able to obtain in the OAU suggests that Black African governments in their turn are likely to look to oil and to Arab support as their most effective means of securing a decisive victory in the confrontation between Black and White in Southern Africa. In response to an appeal from the OAU, the Arab summit conference at Algiers formally extended the oil embargo to South Africa, Mozambique and Portugal and called on Arab countries to break all remaining relations with those countries. The manipulation of supplies of oil (and possibly some other strategic raw materials) may appear an attractive option to radical Third World governments in other disputes between the less developed countries and the industrialized West. But although there are indications of growing Third World solidarity on a range of political and economic issues, it may be questioned how far

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Individual Arab and other major "non-aligned" oil producers would be prepared to respond to appeals to use the oil weapon in support of causes which they might regard as being of secondary importance to them. Moreover, such manipulation of oil supplies would be a two-edged weapon: many developing countries (India is a notable example) are bound to be hard hit by increases in the price of oil and cuts in supplies and there is no certainty that they could be insulated from the ill effects; in addition their economic development would suffer further if the economies of the developed West were seriously disrupted. These factors could cause serious strains between the oil producers and other developing countries.

43. In the short term the West will have little alternative than to reduce energy consumption and seek to minimise the likelihood of further threats to its oil supplies by means of political persuasion and constructive participation in efforts to secure or to maintain an Arab/Israeli settlement. Western efforts to develop alternative sources of energy will of course be greatly intensified: the cuts in supplies and the certainty of escalating prices are likely to overcome scepticism and other constraints which have hitherto inhibited the exploitation of old or unconventional hydrocarbon resources under Western control; and the development of nuclear and perhaps solar energy will be accelerated. The application of technological solutions will take time, and be very costly. The likely gap between projected world energy requirements and planned Middle East oil production has for some time been a cause for concern; the use of oil as a political weapon adds a dangerous new dimension to the problem. But at the same time it will serve to accelerate the development of alternative energy sources which was in any case inevitable and this could help to offset some of the economic loss from shortages of oil.

44. In time a combination of factors is likely to lessen both the potency of the oil weapon and the likelihood of its use: the stabilisation of Arab/Israeli relations; the lessening of Western dependence on oil as alternative supplementary sources of energy are developed; growing economic interdependence between the Arab oil producers and the West, arising from the former's need to invest their large financial surpluses; the

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development of closer economic and political relations generally between the European Community and the countries of the southern Mediterranean and the Middle East. But this presupposes that the advanced Western countries and Western Europe in particular can get through the intervening period, which might last at least 10 years, without crippling economic and political damage.

47. The period of vulnerability should be shorter in the case of the United Kingdom. If all goes well, the British sector of the North Sea will be yielding about 100 million tons of oil a year by 1980, and significant flows could be obtained earlier by an intensive national effort. North Sea oil could by 1980 provide two-thirds of our needs of that date as historic estimates, and if high world oil prices led to reductions in demand, this proportion could be significantly higher. We should thus have a reasonable prospect of being able to meet almost all our oil needs from North Sea and non-Arab sources (Iran, Nigeria and Venezuela). However, although North Sea oil can be adapted to many uses, it could be advantageous for us to export some of it as long as the quantity exported, eg to continental Europe, was balanced by imports of different qualities of oil from elsewhere. This help from the North Sea should last us at least until the 1990s and thereafter nuclear supplies could be making an important contribution to our energy needs.

48. Though we are better placed than most and though the period of risk is difficult to estimate with accuracy, there will certainly be a period of risk in which the United Kingdom and other Western countries will remain crucially dependent upon Middle East oil. This uncertain situation will pose major problems both for relations between Europe and the United States and for the cohesion and development of the European Community. For Western Europe key questions will include -

- a. The extent to which differing European and United States perceptions of the Arab/Israeli dispute and differing degrees of United States and European vulnerability to Arab oil pressure will be allowed to undermine the wide range of common Atlantic interests.

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- b. The extent to which Western Europe and Japan, individually or collectively, will give way to further Arab pressure in the Arab/Israeli conflict or over such issues as preferential economic arrangements between oil producer and consumer governments.
- c. The extent to which individual member governments of the Community will concentrate on safeguarding for themselves their national and technological sources of energy or will be prepared to co-operate with their partners in developing an effective common energy policy.

7 December 1973

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